Agenda Date: 01/23/04
Agenda Item: 4B

STATE OF NEW JERSEY
Board of Public Utilities
Two Gateway Center
Newark, NJ 07102
www.bpu.state.nj.us

TELECOMMUNICATIONS

IN THE MATTER OF THE BOARD'S REVIEW OF UNBUNDLED NETWORK ELEMENTS RATES, TERMS AND CONDITIONS OF BELL ATLANTIC-NEW JERSEY, INC.	)))))	ORDER DENYING MOTIONS

BPU DOCKET NO. TO00060356

(SERVICE LIST ATTACHED)

BY THE BOARD:

By this Order, the Board of Public Utilities ("Board") considers the emergency petition filed on December 29, 2003 by AT&T Communications of NJ, L.P. ("AT&T")[1] for reconsideration of the Board's December 23, 2003 Order ("Review Order") [2] and the letter motion filed on December 30, 2003 by MCImetro Access Transmission Services, L.L.C. ("MCI")[3] requesting that the Board hold in abeyance all proceedings announced in the Review Order. The Review Order memorialized action taken by the Board at its December 17, 2003 Agenda Meeting, whereby the Board announced its intention to reopen its review of two inputs, specifically, cost of capital and depreciation, which affect the rates at which Verizon New Jersey, Inc. ("VNJ", formally known as Bell Atlantic-New Jersey, Inc.), is required to provide unbundled network elements ("UNEs") to Competitive Local Exchange Carriers ("CLECs") pursuant to the Federal Communications Commission ("FCC") Local Competition rules.

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[1] AT&T's December 29, 2003 Emergency Petition filed with the Board, for Reconsideration of Order Reopening Proceeding in Docket Number TO00060356 ("AT&T's Motion for Reconsideration").

[2] See Order, I/M/O the Board's Review of Unbundled Network Elements Rates, Terms and Conditions of Bell Atlantic-New Jersey Inc., Docket No. TO00060356 (Dec. 23, 2003) (" Review Order").

[3] December 30, 2003 Letter Motion of MCI filed with the Board, to hold in abeyance all further proceedings in Docket Number TO00060356 ("MCI's Motion for a Stay").

MOTIONS

While the arguments set forth in support of AT&T's Motion for Reconsideration, MCI's Motion for a Stay and VNJ's responses thereto are more fully discussed in the Discussion and Findings section below, the following is a synopsis of the arguments raised by each of the parties in this regard.

AT&T's Motion for Reconsideration

On December 29, 2003, AT&T filed with the Board its emergency petition for reconsideration, reversal or modification of the Review Order, reopening the UNE proceeding on two issues. In support of its motion, AT&T argued that the Triennial Review Order[4] issued by the FCC on August 21, 2003, "imposes no obligation on the Board to reopen the record on either the depreciation or cost of capital issue."[5] AT&T asserted that reopening the proceeding on the two issues and in the time frame allotted in the Board's Review Order, did not comply with "the TELRIC standard and general norms of administrative due process." AT&T further argued that if the Board decides to "proceed with reopening, both the scope and the timetable of reopening must be expanded."[6]

VNJ's Response to AT&T's Motion for Reconsideration[7]

VNJ responded to AT&T's motion, asserting that the Board may lawfully review the depreciation and cost of capital input assumptions without reviewing all "cost inputs" that it previously set in light of the "FCC's recent clarification of the standards that *should have* been applied by the Board" on these two issues.[8] VNJ also argued that the schedule set by the Board for the reopened proceeding was sufficient based upon the narrow issues to be reviewed, and because during the Board's "Generic Proceeding, the cost of capital and depreciation issues were addressed completely over two hearing days and in fourteen pages of the Board's 279-page decision."[9]

AT&T's Reply to VNJ's Response to AT&T's Motion for Reconsideration

In AT&T's January 13, 2004 reply to VNJ's Response to its Motion for Reconsideration, AT&T argued that VNJ failed to explain why the Board should reopen the proceeding on two issues "while setting in stone all other cost inputs—despite evidence that several

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[4] Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers, Federal Communications Commission, CC Docket Nos. 01-338, 96-98-98-147 (rel. Aug. 21, 2003) ("TRO").

[5] AT&T's Motion for Reconsideration at 1.

[6] AT&T's Motion for Reconsideration at 1.

[7] On January 21, 2004, VNJ filed a surreply brief and indicated that it had no objection to the Board treating the letter brief as supporting a motion for leave to file a surreply brief. However, because general motion practice procedures do not allow for surreply motions without leave of the court (or here the Board), the Board does not take into consideration VNJ's surreply brief in this Order. See New Jersey Court Rule 1:6-3(a).

[8] VNJ's January 9, 2004 Response to AT&T's Motion for Reconsideration at 2-3.

[9] VNJ's January 9, 2004 Response to AT&T's Motion for Reconsideration at 3.

have declined significantly since the close of the previous record."[10] AT&T also argued that because of VNJ's *ex parte* communications with the Board, no other party had an advance notice or opportunity to comment on the effect the proper scope of reopening before the Board acted.[11] Moreover, AT&T argued that when VNJ gained the Board's and FCC's authorization to provide interLATA service in New Jersey, VNJ never challenged the depreciation or cost of capital inputs and agreed not to challenge UNE rates, and therefore the Board should estop VNJ "from seeking to relitigate its UNE prices now."[12]

MCI's Motion for a Stay

On December 30, 2003, MCI filed its Motion for a Stay claiming that the Board did not have jurisdiction to reopen this matter because it is the subject of a pending appeal and that it is not feasible to determine costs for UNEs "when the list of available UNEs is currently undergoing review by the Board and may very well change by July 2, 2004."[13] Thus, MCI requested that the Board hold all further proceedings in this docket in abeyance until after either the resolution of the pending appeals in District Court, including MCI's appeal concerning the Board's Order on Reconsideration in this matter, and "the completion of the nine month Triennial Review Order proceeding now pending before the Board in Docket No. TO0309705."[14] In addition to the motion to hold in abeyance, MCI further sought determination by the Board that when it reopens the UNE case, the proceeding will "include an examination of the cost model, all current inputs and other data needed to develop a current TELRIC rate, in accordance with applicable FCC requirements."[15]

VNJ's Response to MCI's Motion for a Stay

On January 12, 2004, VNJ responded to MCI's Motion for a Stay. VNJ argued that the Board does not lack jurisdiction to reopen its UNE rate proceeding because the Board's and VNJ's agreement to seek dismissal of VNJ's District Court claims freed the Board to reopen discrete aspects of the UNE rate proceeding.[16] VNJ also argued, "because the Board has not made any findings of fact or conclusions of law regarding rate adjustments, the Board has not usurped any jurisdiction from the District Court."[17] VNJ further claimed that federal precedent allows for the "reopening of an administrative proceeding during the pendency of an appeal in federal court," and that if the Board

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[10] AT&T's January 13, 2004 Reply on Motion for Reconsideration at 1.

[11] AT&T's January 13, 2004 Reply on Motion for Reconsideration at 2.

[12] AT&T's January 13, 2004 Reply on Motion for Reconsideration at 11, citing Application of Verizon New Jersey, Inc., et al., for Authorization to Provide In-Region InterLATA Services in New Jersey, 17 FCC Rcd 12275 (2002) at ¶¶15-73.

[13] MCI's Motion for a Stay at 1.

[14] MCI's Motion for a Stay at 1.

[15] MCI's Motion for a Stay at 1.

[16] VNJ's January 12, 2004 Response to MCI's Motion for a Stay at 3.

[17] VNJ's January 12, 2004 Response to MCI's Motion for a Stay at 2.

holds reopening until resolution of the District Court matter and the TRO proceeding, it would result in "the perpetuation of the unreasonably low UNE rates established by incorrect application of the cost of capital and depreciation assumptions."[18] With regard to arguments raised by both AT&T and MCI, VNJ incorporated its arguments in response to AT&T's Motion for Reconsideration.

MCI's Reply to VNJ's Response to its Motion for a Stay

On January 22, 2004, MCI filed a reply to VNJ's Response to MCI's Motion for a Stay, arguing that the federal decisions relied upon by VNJ in support of its claim that the Board has the ability to reopen a docket while an appeal is pending "actually support MCI's position that the Board lacks jurisdiction at the present time."[19]

Upon a thorough review of the motions, and for the reasons detailed herein, the Board finds that the motions filed by AT&T and MCI should be **DENIED** in their entirety.

BACKGROUND

By way of Order issued on December 2, 1997, the Board set its initial rates, terms, and conditions for access to UNEs consistent with the Total Element Long Run Incremental Cost ("TELRIC") methodology articulated by the FCC in its Local Competition Order. [20] Following the release of the Board's Generic Order, AT&T challenged the Board's decision in District Court.[21] On June 6, 2000, the United States District Court for the District of New Jersey issued a decision that affirmed in part, reversed in part, and remanded in part issues addressed in the Generic Order.[22]

The Board's review on remand was completed on November 20, 2001.[23] The Final Order, issued March 6, 2002, adopted modified inputs and assumptions used in the cost models to calculate recurring and non-recurring rates, and established the terms and conditions under which certain advanced services would be made available to CLECs. The Final Order reduced many of the wholesale rates that VNJ had been charging CLECs pursuant to the Generic Order. Following the release of the Board's Final Order, WorldCom, AT&T and the Ratepayer Advocate (RPA) filed motions for reconsideration alleging that the Board had erred in rendering its decision. After a review of the

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[18] VNJ's January 12, 2004 Response to MCI's Motion for a Stay at 2-3.

[19] MCI's January 22, 2004 Reply in support of its Motion for a Stay at 1.

[20] See Decision And Order, In the Matter of The Investigation Regarding Local Exchange Competition For Telecommunications Services, Docket No. TX95120631 (Dec. 2, 1997) ("Generic Order").

[21] See AT&T Communications of New Jersey, Inc., et al. v. Bell Atlantic-New Jersey, Inc., et al., Civ. Nos. 97-5762(KSH) and 98-0109.

[22] See AT&T Communications of New Jersey, Inc., et al. v. Bell Atlantic-New Jersey, Inc., et al., Civ. Nos. 97-5762 and 98-0109 (KSH) (D.C.N.J. June 6, 2000) (hereinafter, AT&T v. BA-NJ).

[23] See Decision and Order, I/M/O the Board's Review of Unbundled Network Elements Rates, Terms and Conditions of Bell Atlantic-New Jersey, Inc., Docket No. TO00060356 (March 6, 2002). ("Final Order").

reconsideration requests, the Board rendered its decision on reconsideration at its July 15, 2002 Agenda Meeting. [24]

Subsequent to the release of the Board's Order on Reconsideration, VNJ filed a Complaint in United States District Court for the District of New Jersey on November 7, 2002, pursuant to the Telecommunications Act of 1996 (47 U.S.C. §252(e) (6)).[25] The Complaint was filed against both the Board and individual commissioners in their official capacities and consisted of three counts. In its Complaint, VNJ requested that the case be remanded to the Board for further review of the inputs and assumptions used to develop the UNE rates for compliance with the FCC's TELRIC methodology. Count One alleged that the UNE rates established by the Board failed to comply with the FCC's TELRIC methodology, as set out in the Act and its implementing regulations. Count Two alleged that the Board's UNE rates are below VNJ's actual costs and that they constitute an unconstitutional taking under the Fifth and Fourteenth Amendments to the U.S. Constitution. Count Three alleged that the Board's action further constituted a violation of VNJ's civil rights under 42 U.S.C. §1983. The Board filed an Answer to VNJ's Complaint on December 23, 2002.[26] On March 28, 2003, MCI filed an Answer, Counterclaim and Cross-Claim for Declaratory and Injunctive Relief with the District Court ("MCI's Counterclaim").[27]

Subsequently, on November 26, 2003, VNJ Filed a Motion for Leave to File and Serve an Amended Complaint expanding its Complaint to include three additional counts. Proposed Counts Four and Five alleged that the UNE rates established by the Board

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[24] See Decision and Order, I/M/O the Board's Review of Unbundled Network Elements Rates, Terms and Conditions of Bell Atlantic-New Jersey, Inc., Docket No. TO00060356 (September 13, 2002). ("Order on Reconsideration").

[25] Verizon New Jersey Inc. v. the New Jersey Board of Public Utilities, an agency, and Jeanne M. Fox, in her official capacity as President of the New Jersey Board of Public Utilities, Frederick F. Butler, in his official capacity as Commissioner of the New Jersey Board of Public Utilities, Connie O. Hughes, in her official capacity as Commissioner of the New Jersey Board of Public Utilities, Carol J. Murphy, in her official capacity as Commissioner of the New Jersey Board of Public Utilities, and Jack Alter, in his official capacity as Commissioner of the New Jersey Board of Public Utilities, Civil Action No. 02-5353 (JAP). MCI filed a Counterclaim and a Cross-claim on December 20, 2002. This action is still pending in District Court, and VNJ and the Board have filed Answers to MCI's Counterclaim and Cross-claim. By Orders dated March 21, 2003, the Court granted AT&T leave to intervene as intervenors and RPA leave to participate as *amicus curiae*.

[26] On February 25, 2003, the Board filed a Motion to Dismiss Counts Two and Three. Supporting and responsive briefs were also filed with regard to that Motion to Dismiss Counts Two and Three.

[27] In its Counterclaim, MCI appealed the Board's Final Order and Order on Reconsideration and the Board's Order Approving Interconnection Agreement, In re Petition for Arbitration of Unresolved Issues Pursuant to Section 252(e) of the Telecommunications Act of 1996, Docket No. TO96080621 issued on November 20, 1997 ("Approval Order") as violative of the Telecommunications Act of 1996. Specifically, in ¶92 of its Counterclaim, MCI alleged in Count One that the Board's adoption of VNJ's "loop pricing model violates the FCC's TELRIC pricing methodology and the 1996 Act because that model is based on Verizon's existing network, rather than a network designed with the most efficient technology or lowest cost network configuration." See MCI's Counterclaim at 21. In Count Two, MCI alleged that contrary to the 1996 Act and law, "the Board accepted Verizon's unlawful assumption that only 60% of the loop plant in its actual network would be DLC ["Digital Loop Carrier"], and that the remaining 40% would be inefficient end-to-end copper loops." See MCI's Counterclaim at 22. In Count Three, MCI claimed that "the Board's approval of Verizon's building and land factors, and of Verizon's use of an FLC ["Forward-Looking-to-Current"] factor in adopting these expense factors, overstated the costs of providing elements based on a proper forward-looking TELRIC-compliant network… [and] the Board approved Verizon's inflated land and building factors…" which MCI claimed "unlawfully inflated Verizon's UNE rates far in excess of the forward-looking costs permitted under the Act and FCC's regulations." See MCI's Counterclaim at 23. In Count Four, MCI alleged that the Board's "adoption of a two-tiered switching rate based on MOU ["minutes-of-use"] violates the 1996 Act and the FCC's implementing regulations…." MCI indicated that it has been "aggrieved by the Board's failure to adopt a flat rate switching design." See MCI's Counterclaim at 25.

violate the Fifth and Fourteenth Amendments on additional grounds. Proposed Count Six alleged that the UNE rates adopted by the Board in the Order on Reconsideration are inconsistent with the Board's findings and are arbitrary, capricious, and unreasonable. MCI, AT&T and the Board filed responses to the proposal by VNJ to amend its Complaint.

During the pendency of the litigation involving VNJ and the Board in the District Court of New Jersey, on August 21, 2003, the FCC released its TRO, providing new, additional guidance to states that may affect the UNE rates established by the states in following the FCC's TELRIC-methodology. The FCC provided clarification on two key inputs used by states to set TELRIC-compliant rates: depreciation and cost of capital. Due to the fact that VNJ's complaint was implicitly premised on its belief that these key inputs are not TELRIC compliant, the Board Staff entered into negotiations with VNJ to discuss the practicality of reviewing these inputs for TELRIC compliance as part of a joint settlement.

On December 19, 2003, VNJ and the Board[28] entered into a Stipulation and Agreement whereby VNJ and the Board agreed to seek leave of the District Court of New Jersey to dismiss VNJ's Complaint, without prejudice, in exchange for an expedited review by the Board of the above-mentioned inputs that were used to calculate the current rates associated with UNEs that VNJ is required to provide to CLECs.

In accordance with the terms of the Settlement and Agreement, and following a December 17, 2003 Agenda Meeting announcing its decision, the Board issued its Review Order on December 23, 2003, directing the reopening of the "UNE proceeding to review the cost of capital and depreciation inputs that were relied upon by the Board in setting the current UNE rates."[29] The Board's Review Order also established a procedural schedule in accordance with the terms of the Stipulation and Agreement requiring an expedited review and Board decision in the reopened UNE proceeding by March 31, 2004.[30]

On December 29, 2003, pursuant to Federal Rules of Civil Procedure 41(a)(2), VNJ filed with the Honorable Joel A. Pisano, United States District Judge for the District Court of New Jersey, a proposed form of Order of Dismissal[31], dismissing without prejudice Verizon NJ's Complaint in accordance with the terms of the Stipulation and Agreement entered into between VNJ and the Board, dismissing the Board's pending motion to dismiss Counts Two and Three of the Complaint, dismissing VNJ's pending motion for leave to file an Amended Complaint without prejudice, and ordering that the District Court of New Jersey shall retain jurisdiction to enforce all provisions and obligations set

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[28] On December 17, 2003, the Board authorized its legal counsel from the Division of Law to execute a Stipulation and Agreement on behalf of the Board in settlement of Verizon's Complaint and Proposed Amended Complaint against the Board and the individual Commissioners in their official capacities.

[29] Review Order at 3.

[30] On January 9, 2004, Commissioner Connie O. Hughes issued an Order reflecting a revised procedural schedule which modified the dates by which parties were to file discovery and testimony, Order, I/M/O the Board's Review of Unbundled Network Elements Rates, Terms and Conditions of Bell Atlantic-New Jersey Inc., Docket No. TO00060356 (January 9, 2004).

[31] VNJ revised and filed a proposed form of Order with the District Court of New Jersey on January 14, 2004, to reflect dismissal of the Board's pending motion to dismiss Counts Two and Three of VNJ's Complaint and dismissal of VNJ's Motion to Amend its Complaint.

forth in the Stipulation and Agreement entered into between VNJ and the Board. MCI and AT&T both filed letters with the District Court, stating that while they did not oppose the District Court's dismissal of VNJ's Complaint and Amended Complaint without prejudice, they had objection to the District Court's approval of the terms of the Stipulation and Agreement.[32] On January 14, 2004, having considered the arguments raised by counsel for AT&T and MCI, Judge Pisano entered an Order dismissing VNJ's Complaint and pending Amended Complaint without prejudice, dismissed without prejudice the Board's pending motion for dismissal of Counts Two and Three of VNJ's Complaint, and retained jurisdiction to enforce all provisions and obligations set forth in the Stipulation and Agreement entered into between VNJ and the Board.[33]

DISCUSSION AND FINDINGS

MCI's Claim that the Board Has No Jurisdiction to Reopen the UNE Proceeding

In its Motion for a Stay, MCI claimed that the Board lacked jurisdiction to reopen the UNE proceeding as set forth in the Board's Review Order. In support of this proposition, MCI cited primarily to New Jersey case law that purport that the pendency of an appeal divests the Board of jurisdiction over the subject matter of the appeal.[34] In its reply, MCI discussed the federal cases VNJ had discussed in its response in support of its position that the federal cases actually supported its position since the reopened proceeding "is not going to provide MCI a fair opportunity to present its case for a TELRIC-compliant rate."[35]

In response to MCI's Motion, VNJ argued that the Board and VNJ jointly requested that the District Court dismiss VNJ's complaint and to remand the case to the Board to determine if the Board applied the correct legal standard when establishing specific assumptions when setting the existing UNE rates. Under federal law, an administrative agency may move to assert jurisdiction over a case within its jurisdiction during the pendency of a federal appeal if appropriate. The Board has not made any findings of fact or conclusions of law regarding rate adjustments or its previously rendered decision concerning existing UNE rates. It is not uncommon for the Board to review aspects of a

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[32] See AT&T's December 31, 2003 letter brief and MCI's January 8, 2004 letter in response to VNJ's December 29, 2003 motion requesting that District Court Judge Pisano enter a proposed order dismissing VNJ's Complaint in Docket No. 02-CV-5353 (JAP).

[33] See January 14, 2004 Order issued by Judge Pisano in Verizon New Jersey Inc. v. the New Jersey Board of Public Utilities, an agency, and Jeanne M. Fox, in her official capacity as President of the New Jersey Board of Public Utilities, Frederick F. Butler, in his official capacity as Commissioner of the New Jersey Board of Public Utilities, Connie O. Hughes, in her official capacity as Commissioner of the New Jersey Board of Public Utilities, Carol J. Murphy, in her official capacity as Commissioner of the New Jersey Board of Public Utilities, and Jack Alter, in his official capacity as Commissioner of the New Jersey Board of Public Utilities, Civil Action No. 02-5353 (JAP).

[34] MCI's Motion for a Stay at 2, citing R. 2:9-1; Manalapan Realty L.P. v. Manalapan Township Committee, 140 N.J. 366, 376 (1995); Ledezma v. A&L Drywall, 254 N.J.Super. 613, 619 (App. Div. 1992); In re Plainfield-Union Water Co., 14 N.J. 296, 302 (1954).

[35] MCI's January 22, 2004 Reply in support of its Motion for a Stay at 2-3, citing Anchor Line Ltd. V. Federal Maritime Comm'n, 299 F.2d 124, 125 (D.C. Cir. 1962)("Anchor Line"); B.J. Alan Co., Inc. v. ICC, 897 F.2d 561 (D.C. Cir. 1990); B.J. American Farm Lines v. Black Ball Freight Service, 397 U.S. 532, 541-42 (1970); Steel Co. v. United States, 306 U.S. 153, 160 (1939).

prior decision. In doing so, contrary to MCI's claims, the Board has not usurped jurisdiction from the District Court."[36]

The Board has reviewed the arguments raised by MCI on the issue of the Board's jurisdiction to reopen the UNE proceeding to review the cost of capital and depreciation issues. In support of its claim that the Board acted to reopen without jurisdiction, MCI relied upon (among other cases) Manalapan Realty, L.P. v. Township Committee of Tp. of Manalapan, 140 N.J. 366 (1995), where the Supreme Court of New Jersey stated that "[t]he ordinary effect of the filing of a notice of appeal is to deprive the trial court of jurisdiction to act further in the matter unless directed to do so by an appellate court, or jurisdiction is otherwise reserved by statute or court rule,"[37] and upon R. 2:9-1(a), and its federal analog 28 U.S.C.A. §2347, which provides that "[o]nce a petition to review has been filed in court, the FCC has no authority to conduct further proceedings without the court's approval."[38] This case does not affect the procedural posture of the Board's proceeding as set forth in the Review Order. Here, VNJ withdrew its claims against the Board and the Board and VNJ sought leave of the District Court for dismissal of the action, and for divestiture of jurisdiction pursuant to Federal Rule of Civil Procedure 41(a)(2).[39] The District Court entered an Order divesting itself of jurisdiction with regard to VNJ's complaint against the Board, subject to enforcing the terms of the Stipulation and Agreement.[40] Thus, the purposes of the cases and rules cited by MCI have been fulfilled -- the higher court has divested jurisdiction to the Board to reopen the proceeding.

While MCI correctly noted that the Review Order set forth a procedural schedule on the reopened proceeding prior to the District Court's decision on VNJ's and the Board's motion for entry of a Proposed Order of Dismissal, the Board commenced with the reopening of the proceeding for purposes of expedience of the administrative process with regard to the discreet issues on review. In any event, even if action by the District Court should have preceded any action by the Board to commence the reopened proceeding, the Board's issuance of the Review Order prior to the District Court's issuance of its Order of January 14, 2004 was not prejudicial.[41] Therefore, there is no usurpation of the District Court's jurisdiction in the Board's reopening of the UNE proceeding on the issues discussed in the Board's Review Order. Furthermore, the Board has sought to reopen the proceeding pursuant to guidance from the FCC on cost of capital and depreciation, guidance that the Board deems directly relevant to its prior decision as set forth in its Final Order. The Board "at any time may order a rehearing

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[36] VNJ's Response to MCI's Motion at 2.

[37] Manalapan Realty, L.P. v. Township Committee of Tp. of Manalapan, 140 N.J. at 376 (citations omitted).

[38] See MCI's Motion for a Stay at 2.

[39] See VNJ's December 29, 2003 Motion for the District Court to enter a proposed form of Order of Dismissal.

[40] See Judge Pisano's January 14, 2004 Order.

[41] In Anchor Line, it was held that the Commission's failure to move before the court to remand or hold in abeyance or otherwise for authority to reopen a proceeding of which the review was pending was not prejudicial.

and extend, revoke, or modify an order made by it."[42] The Board is guided by the FCC's determination that "[w]e conclude that it is necessary to clarify the application of two components of TELRIC that have a major impact on UNE prices – cost of capital and depreciation."[43]

Moreover, MCI's pending District Court appeal does not specifically implicate either the cost of capital and depreciation issues to be reviewed pursuant to the Review Order on the basis on new guidance from the TRO.[44] VNJ contended that the FCC's guidance suggests that the Board may have improperly applied the cost of capital and depreciation assumptions, and that if the District Court "ultimately determines that the Board erred in applying TELRIC principles as alleged by MCI, MCI's remedy will be a court-ordered remand to the Board."[45] MCI's Counterclaim is still pending with the District Court. Therefore, the Board has authority to reopen and review the cost of capital and depreciation issues, and any determination made by the District Court regarding MCI's claims will control the Board's resulting action with regard to MCI's pending appeal.

Thus, the precedent cited by MCI is not applicable to this case as VNJ and the Board has received the District Court's authority to act in accordance with the terms of the Stipulation and Agreement and reopen the proceeding on two issues that are not the basis of MCI's Counterclaim in the pending federal action. Accordingly, the Board **HEREBY DENIES** MCI's request that the Board hold the reopened UNE proceeding in abeyance on the basis that it has no jurisdiction to reopen.

MCI's Claim that the Board Must Wait for the TRO Proceeding to Conclude

MCI also argued that the Board must hold in abeyance its decision to reopen "until the conclusion of the TRO case, scheduled to occur no later than July 2, 2004, before it begins the process of establishing new UNE rates," because "the costs of certain UNEs which were purportedly included in the old Verizon cost model will need to be removed from the cost model if the UNEs themselves will no longer be available, or will be available only in limited geographic areas."[46] Additionally, MCI argued that the FCC's decision in the TRO may have implications for the cost of capital and depreciation and

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[42] N.J.S.A. 48:2-40. See also Mutschler v. New Jersey Dep't of Env. Protection, 337 N.J.Super. 1, 14 (App. Div. 2001); Busse Broadcasting Corp. v. FCC, 87 F.3d 1456, 1465 (D.C. Cir. 1996).

[43] TRO at ¶ 675.

[44] See footnote 24, supra. Also, in MCI's January 8, 2004 letter response to Judge Pisano regarding VNJ's December 29, 2003 motion for entry of a proposed order, MCI claimed that its "own appeal must go forward" and essentially provides a synopsis of its arguments on appeal pursuant to its Counterclaim, currently pending with the District Court. Specifically, MCI asserted that the Board's intent to reopen on cost of capital and depreciation "will only compound the errors the Board made when it used Verizon's non-TERLIC compliant cost model, when it used an unreasonable split between digital and copper telephone lines (loops), when it inflated land and building-related costs through the so-called 'FLC factor,' and when it rejected MCI's proposal for a flat rate for switching." MCI's January 8, 2004 letter response to Judge Pisano at 2.

[45] VNJ's January 12, 2004 Response to MCI's Motion for a Stay at 7.

[46] MCI's Motion for a Stay at 3.

other costing issues.[47] MCI further claimed that because the TRO is also pending appeal at the U.S. Court of Appeals for the D.C. Circuit and is scheduled for argument on January 28, 2004, "it is not feasible to engage in any ratemaking for UNEs before then."[48]

In response, VNJ essentially argued that MCI would have the Board await resolution of all the cited pending appeals, which could to take years to resolve, rather than reopening the proceeding on the two issues, which it claims that the Board should review and potentially correct if they are found to be set in error.[49]

The Board's joint settlement with VNJ entailed a review of the cost of capital and depreciation issues because the FCC had provided specific guidance on those two issues, and those two issues were also the subjects of VNJ's appeal in District Court. Without admitting any error in the rates set in its prior orders in the underlying proceedings, the Board agreed to review these assumptions given the clear guidance from the FCC. The Board has agreed to conduct a review of these assumptions and has set a schedule of a proceeding that provides all parties the opportunity to review and comment on these two issues. Any further guidance from the FCC and the appellate courts would likely guide this Board's future action and determinations. MCI is not prejudiced by the reopening of these two issues while the TRO proceedings and appeal are pending. Accordingly, the Board **DENIES** MCI's request for a Stay until all TRO related appeals and matters are fully resolved.

AT&T's Claim that the TRO does not Justify Reopening

AT&T argued in its Motion for Reconsideration that there is no reason to reopen this proceeding on the issue of depreciation because the depreciation lives adopted by the Board in its March 2002 Final Order are consistent with the TRO.[50] AT&T claims that while "the basic issue raised by the parties on the record before the Board in 2000-2001 was whether regulatory depreciation lives or financial ("GAAP") lives provide a better measure of forward-looking economic depreciation lives," the Board found that regulatory lives were the better benchmark.[51] AT&T argued that the guidance provided in the TRO does not require a change in the Board's findings, and the evidence provided by VNJ to support the use of GAAP depreciation lives during the 2001-2002 proceeding did not demonstrate with any detail, study or testimony that GAAP lives are a more appropriate measure of the actual economic life of an asset.

In response to this claim, VNJ asserted that in the Final Order, the Board adopted "allegedly 'forward looking' depreciation rates" that were established prior to the adoption of the Telecommunication Act of 1996, and because the rates were established before

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[47] MCI's Motion for a Stay at 3.

[48] MCI's Motion for a Stay at 3.

[49] VNJ's January 12, 2004 Response to MCI's Motion for a Stay at 8.

[50] AT&T Motion for Reconsideration at 4.

[51] AT&T Motion for Reconsideration at 4, citing Docket No. TO00060356, Decision and Order (served March 6, 2002) at 40-45.

"TELRIC came into existence, there can be little doubt that TELRIC competitive assumptions were not applied."[52]

With regard to the cost of capital issue, AT&T claimed that the TRO did in fact change the standard in effect in 2002, and as applied by the Board's Final Order, however this change "cannot be given retroactive effect on review" of the Board's Final Order.[53] In support of the assertion that the TRO has changed the cost of capital standard, AT&T cited to the FCC's 1996 Local Competition Order[54] where the FCC provided that the "required return on investment would be defined by the 'business risks that' the incumbents 'face'—an obvious reference to the risks that incumbents actually anticipate, not the risks of a hypothetical competitive market".[55] AT&T claimed that it was pursuant to this standard that "state commissions generally found in recent years that the relevant cost of capital for UNEs was in the range of nine or ten percent."[56] Moreover, AT&T argued that even if the cost of capital standard set forth in the TRO is applied here, there is no reason to believe that applying the FCC's cost of capital standard would result in raising the cost of capital.[57]

In response, VNJ claimed that the Final Order failed to account properly for the effects of competition when establishing the cost of capital level, whereas the "FCC's recent clarification makes it abundantly clear that when setting the cost of capital the Board *was required* to assume a fully competitive market."[58] With regard to AT&T's assertion that the TRO has changed the standard for determining the appropriate cost of capital, VNJ responded that the TRO does not change the rules, but rather it "clarifies the existing TELRIC rules and interprets the Local Competition Order, which was in effect at the time of the Board's UNE decision."[59]

To the extent that AT&T claimed that the Board correctly applied depreciation whereas VNJ claims that the Board did not, and where the Board has received guidance on this issue from the FCC[60], the Board will review the merits of these issues during the reopened phase of this proceeding and when all parties have issued their testimony to support their relative positions with regard to the issue of depreciation. Similarly, with regard to cost of capital, while AT&T claims that the FCC has changed the law and VNJ

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52 VNJ's January 9, 2004 Response to AT&T's Motion for Reconsideration at 7.

53 AT&T Motion for Reconsideration at 7.

54 First Report and Order, In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996 (CC Docket No. 96-98); Interconnection between Local Exchange Carriers and Commercial Mobile Radio Service Providers (CC Docket No. 95-185), FCC No. 96-325, ¶702 (rel. Aug. 8, 1996) ("Local Competition Order"), aff'd in relevant part, Verizon Communications Inc. v. FCC, 535 U.S. 467 (2002).

55 AT&T's Motion for Reconsideration at 8.

56 AT&T's Motion for Reconsideration at 8.

57 AT&T Motion for Reconsideration at 11.

58 Verizon's January 9, 2004 response to AT&T's Motion for Reconsideration at 7.

59 Verizon's January 9, 2004 response to AT&T's Motion for Reconsideration at 8.

60 The FCC stated in its TRO that the depreciation rate "should reflect the actual decline in value that would be anticipated in the competitive market TELRIC assumes." TRO at ¶ 689.

asserts that the Board did not assume a fully competitive market as it was then required, the FCC expressly stated that "states should establish a cost of capital that reflects competitive risks associated with participating in the type of market that TELRIC assumes."[61] Thus, the Board has guidance from the FCC on these two issues. The FCC is currently reviewing the entire TELRIC procedure in a separate proceeding and when concluded, should provide further guidance to the Board on the UNE rates it has set.[62] Therefore, the Board **HEREBY DENIES** AT&T's Motion for Reconsideration on the basis that the TRO does not warrant reopening of the proceeding.

AT&T's and MCI's Claim that the Board's Review should be Expanded

MCI claimed that given the Seventh Circuit's decision in AT&T Communications of Illinois, Inc. v. Illinois Bell Telephone Co., 349 F.3d 402 (7th Cir. 2003)("AT&T 7th Circuit Decision"), the Board's review as contemplated in its Review Order "cannot possibly yield rates that are TELRIC-compliant."[63] MCI asserts that "when the Board does proceed to reexamine UNE rates during the second half of this year (assuming MCI's appeal is resolved by then)…it will need to incorporate into its analysis whatever further guidance may issue from the federal court. It will need to examine, the cost model, costs and set rates for the universe of UNEs that will actually be available in light of the BPU's TRO proceeding and the appeals of the FCC's TRO decision. And it will need to look at all current data for all relevant costs, rather than trying to blend stale data for some inputs with more current data for just two others."[64]

AT&T also claimed that if reopened, the proceeding must be broadened to allow consideration of all material changes in costs since the close of the previous record. AT&T argued that the Board cannot lawfully examine only two factors of the TELRIC rate in isolation from the other components of the overall rate, and because rates established under TELRIC are "the composite of many diverse factors and one 'factor, which elevates the rate, may be offset by other factors that depress it.'"[65]

In support of the contention that two factors "cannot be evaluated in isolation from the other components of a TELRIC rate"[66], both AT&T and MCI cite to the AT&T 7th Circuit Decision. However, upon a review of the 7th Circuit's decision, it is clear that the basis for the holding in that case is not analogous to the Board's proceeding here. In the AT&T 7th Circuit Decision, the Illinois legislature enacted a statute that the Illinois Commerce Commission ("ICC") was mandated to use (despite the ICC's discontent with

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61 TRO at ¶ 681.

62 See In the Matter of the Commission's Rules Regarding the Pricing of Unbundled Network Elements and Resale of Service by Incumbent Local Exchange Carriers, Docket No. WC 03-173.

63 MCI's Motion for a Stay at 4.

64 MCI's Motion for a Stay at 4.

65 AT&T's Motion for Reconsideration at 13, citing AT&T 7th Circuit Decision, 349 F.3d at 408.

66 AT&T's Motion for Reconsideration at 13, citing AT&T 7th Circuit Decision, 349 F.3d at 411.

the statutory restrictions that it was mandated to apply[67]) in determining the rates that the incumbent local telephone company could charge competitors. The statute set forth the rates that the incumbent carriers were to charge the other carriers for unbundled loops, and directed that the ICC to employ actual "fill factors (the proportion of a facility or element that will be 'filled' with network usage)" that reflected the actual total usage in establishing cost based rates for the UNEs.[68] The statute also directed the ICC to "employ depreciation rates that are forward-looking" economic lives.[69] The statute required the rate adjustments to "be completed within 30 days of the effective date" of the law.[70] Prior to the ICC's application of the statute, the competitive carriers filed suit in district court arguing that the Telecommunications Act of 1996 preempted the legislation.[71] The district court granted the injunction requested by the competitive carriers and enjoining the implementation of the statute, holding that the statute was defective for two reasons- federal law "makes the state regulatory commission the exclusive source of non-federal substantive rules" and because the statutory requirement for the handling of fill factors and depreciation conflicted with TELRIC.[72] The incumbent carrier appealed this decision to the United States Court of Appeals for the Seventh Circuit. By the time the district court decision had been issued, the ICC had applied the law because it only had 30 days to implement it.[73]

The United States Court of Appeals for the Seventh Circuit noted that the "decision to file suit before the ICC had applied the statute and announced new rates" caused a procedural problem, because "Congress provided for federal judicial review of rates set by state commissions; it did not provide for review of individual factors that influence those rates."[74] Thus, the Court of Appeals stated, "review of agency action usually is limited to the agency's final decision, and the choice of one or two legal criteria that the agency will use along the way cannot be called a 'final' decision."[75] With regard to the application of the law by the ICC, the Seventh Circuit noted that "the ICC took as set in stone all ingredients of ratemaking from 1997, and it adjusted the rate only by changing the fill factors and asset lives. That approach conflicts with the 1996 Act and the TELRIC methodology and is therefore preempted."[76]

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67 See AT&T 7th Circuit Decision, 349 F.3d at 409 (where it is noted that the Commissioners of the ICC did not favor the law while the Governor did, and the ICC never appealed the District Court's decision to the Seventh Circuit).

68 Id. at 407.

69 Ibid.

70 Ibid.

71 Id. at 408.

72 Ibid.

73 Id. at 411.

74 Id. at 408.

75 Id. at 409.

76 Id. at 411.

Moreover, the Seventh Circuit disagreed with the district court's finding that the requirement in the statute mandating the use of the current fill factors and prior financial reports violated federal law.[77] However, the Seventh Circuit stated that the district court had only considered the two factors on challenge, "but under TELRIC they can't be the only factors, and their propriety should not have been evaluated in isolation from the other components of a TELRIC rate."[78]

Clearly, the situation culminating to the AT&T 7th Circuit Decision is not at all on par with the Board's reopening in this UNE proceeding. In that case, the state statute (rather than the agency) established rules for setting UNE rates, a violation of federal law. Here, the Board is not setting new rules, but is simply reopening the rate proceeding on the two issues to determine compliance with FCC guidelines. Also, in that case the statute restricted the agency's discretion in establishing UNE rates and mandated fixed input assumptions without regard to whether they complied with forward-looking TELRIC standards. That is not the case here; the Board's Review Order directs the parties to provide cost model runs with revised cost of capital and depreciation inputs utilizing the previously approved cost models. Thus, the Board will not simply consider the two factors in isolation, but will review the entire cost model run results that will be derived from the revised cost of capital and depreciation inputs. The other parties will also have an opportunity to perform alternative cost model runs utilizing VNJ's cost models for the Board's consideration. Therefore, AT&T's and MCI's reliance on the AT&T 7th Circuit Decision is misplaced as it relates to this case, and does not warrant the Board's reconsideration of the Review Order.

In support of its Motion for Reconsideration, AT&T also listed all the variables that have changed since the TELRIC rate was established by the Board in its 2002 Final Order, stating "almost every factor affecting the cost of local telephony in New Jersey has changed in the intervening four, five, six or more years since these data were collected."[79] In support of this contention, AT&T made reference to the Loop Cost Analysis Model ("LCAM") used by VNJ and accepted by the Board in its Final Order,[80] but which was subsequently rejected by the Wireline Competition Bureau of the FCC as inconsistent with TELRIC principles.[81]

The Board notes that while the Virginia Arbitration Order did in fact reject the LCAM because if found that the model was not TELRIC-complaint, the Board found it necessary, in its November 20, 2001 decision (which culminated into its Final Order), to revise numerous inputs utilized in VNJ's models so that they would be TELRIC compliant.[82] Therefore, despite the guidance provided in the Wireline Competition

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77 Ibid.

78 Ibid.

79 AT&T's Motion for Reconsideration at 12-17.

80 AT&T's Motion for Reconsideration at 15, citing Final Order at 16.

81 AT&T's Motion for Reconsideration at 15, citing Virginia Arbitration Order at ¶171; 47 C.F.R. §51.503(b)(1).

82 Final Order at 25-30(where the Board explained the modifications it made to the inputs and assumptions in VNJ's cost model to produce true TELRIC-compliant results).

Bureau's decision, the Board deems that it is not necessary to reopen the proceeding on this issue where the Board ensured that VNJ's LCAM model was TELRIC-compliant.

In its reply, AT&T also cited the Virginia Arbitration Order in support of its contention that alleged changes in law do not warrant reopening of the record.[83] AT&T argued that the Wireline Bureau rejected Verizon-Virginia's attempt to reopen the record based on the Supreme Court's pronouncements on the cost of capital issue in Verizon Communications Inc. v. FCC, 535 U.S. 467 (2002), "and several other decisions by the FCC itself on the same issue."[84] Here, the Board has agreed to reopen on two discreet issues, to permit all parties, to submit testimony based on the TRO's clarification, and to ensure clarification (consistent with what the Virginia Arbitration Order did) that the Board-set rates were TELRIC-compliant pursuant to this.[85]

AT&T also argued that since the Board's Final Order was issued, the FCC also modified its "previous unbundling requirements by drastically curtailing the obligation of incumbent LECs to unbundled the broadband capabilities of their loops," thereby eliminating the incumbent LECS obligation to provide "unbundled access to hybrid loops for the provision of packetized broadband services."[86] However, the UNE rate incorporated in the Board's Final Order are cost associated with a narrowband network and do not incorporate any broadband costs. Therefore, this modification in the TRO does not warrant reopening in this proceeding.

AT&T further argued that "[n]ew developments that may affect the outcome of a rate case happen continually, and costs invariably change between the close of the record and the issuance of the final agency decision. This time lag is inherent in ratemaking generally, and TELRIC-based ratemaking specifically," and that unless extraordinarily significant or unexpected, a change in costs or costing methodologies "does not justify reopening the record in a major rate case to admit new evidence."[87] AT&T cited to two cases in support of its contention that a change in costs does not justify reopening the record.[88] However, the cases cited by AT&T are not on all fours with the situation here. In those cases, the parties sought to reopen rate proceedings due to changed circumstances such as declines in costs of major inputs which do not justify reopening

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[83] AT&T's January 13, 2004 Reply on Motion for Reconsideration at 8.

[84] AT&T's January 13, 2004 Reply on Motion for Reconsideration at 8, citing Virginia Arbitration Order at ¶¶17, 19, 22-23.

[85] Virginia Arbitration Order at ¶5.

[86] AT&T's Motion for Reconsideration at 16, citing TRO at ¶ 285-97; AT&T's January 13, 2004 Reply on Motion for Reconsideration at 6, footnote 5.

[87] AT&T's Motion for Reconsideration at 13, citing Verizon Communications Inc. v. FCC, 535 U.S. 467, 505 (2002); Virginia Arbitration Order, ¶ 21.

[88] AT&T's Motion for Reconsideration at 13-14, citing In the Matter of the Application of Verizon Delaware Inc. (f/k/a Bell Atlantic-Delaware, Inc.) for Approval of its Terms and Conditions Under Section 252(f) of the Telecommunications Act of 1996 *(*Filed December 16, 1996; Reopened June 5, 2002*)*, PSC Docket No. 96-324 Phase II ("Verizon-DE"), (Verizon-DE Findings, Opinion and Order No. 5967 (released June 5, 2002) (where AT&T and several other parties asked the Delaware Public Service Commission to reopen the record of the first generation UNE rate case to consider intervening declines in the costs of several major inputs and Verizon-Delaware successfully opposed this request on the basis that consideration of the specific inputs would require a full consideration of "all rate-impacting issues."); and Virginia Arbitration Order at ¶21(where the Wireline Competition Bureau of the FCC denied Verizon-Virginia to reopen the record to consider further evidence on the cost of capital and a few other inputs.)

the record in a major rate case, whereas in the Review Order the Board noted that it is reopening the proceeding on the only two issues that the FCC clarified in its TRO. The TRO did not clarify any other TELRIC cost study assumption requirements. All parties will have an opportunity to fully support their positions on these two issues, and the District Court has divested itself of jurisdiction on the basis of the Stipulation and Agreement between VNJ and the Board. The Board is cognizant of the issues raised in the prior phase of this proceeding, and the respective positions on all issues, including the issue of the switch port charge. As outlined in the Review Order, all parties will have an opportunity to provide cost model runs with revised cost of capital and depreciation inputs utilizing the previously approved cost models at the time of filing their initial (VNJ) and rebuttal (other interested parties) pre-filed testimony, and to further review all supporting worksheets and documentation utilized by the parties in the development of the proposed rates. Thus, contrary to AT&T's concerns, the Board shall consider all parties' comments in the reopened proceeding.

AT&T's and MCI's Claim that the Procedural Schedule is Unworkable

AT&T and MCI took issue with the expedited process in the reopened proceeding. AT&T claimed that the timetable set here is in contrast with the expanded timetable set in the Board's 2000 phase of this case.[89] AT&T also claimed that "there is no reason to believe that reconsideration of the Board's previous findings on depreciation and cost of capital would justify a material change in those input values-let alone in the UNE prices ultimately calculated."[90] In its response to AT&T's Motion for Reconsideration, VNJ claimed that during the Board's 2000-2001 proceeding on the cost of capital and depreciation issues, testimony was completed in two days.

The schedule is compressed due to the limited issues to be reviewed. The Board's procedural schedule is an attempt to conduct an expeditious review of two discreet issues based on FCC guidance. If the parties follow in good faith the revised procedural schedule set forth in the Review Order, the Board is obligated to, and will be able to issue a decision on March 31, 2004.

AT&T's Claim that All Parties Did Not have an Opportunity to Comment on the Scope of Reopening

AT&T claims that the Board and VNJ's decision to reopen the proceeding on the issues of cost of capital and depreciation were "influenced by off-the-record communications, and that no other party received any notice of, or any opportunity to respond to, those communications," and therefore did not afford the parties procedural fairness.[91] In support, AT&T cited to cases that involved the agency in the role of decision-maker rather than in the role of a defendant to an action before a court of law.[92] AT&T also

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89 AT&T's Motion for Reconsideration at 18.

90 AT&T's Motion for Reconsideration at 18.

91 AT&T's January 13, 2004 Reply on Motion for Reconsideration at 2.

92 AT&T's January 13, 2004 Reply on Motion for Reconsideration at 2, citing New Jersey Racing Comm'n v. Silverman, 303 N.J.Super. 293, 308 (App. Div. 1997); High Horizons Dev. Co. v. State of N.J. Dept. of Transp., 120 N.J. 40 (1990); accord Morgan v. U.S., 304 U.S. 1, 18-19 (1938).

cited In the Matter of Petition for Review of Opinion No. 583 of the Advisory Committee on Professional Ethics, 107 N.J. 230, 240 (1987)("Opinion No. 583") and Matter of Fiorillo Bros. of N.J., Inc., 242 N.J.Super. 667, 676-7 (App.Div. 1990)("Fiorillo"), in support of its assertion that VNJ and the Board's staff "are not exempt from the *ex parte* rules merely because the communications occurred in the context of negotiations to settle VNJ's complaint against the Board" in District Court.[93] In Opinion No. 583, the Supreme Court held that while an administrative case is being heard at the Office of Administrative Law, the prosecuting Deputy Attorney General may consult *ex parte* with the administrative agency head to keep the client agency reasonably informed.[94] The Supreme Court emphasized that the "the focus must be on maintaining the impartiality of the agency head in all cases."[95] In Fiorillo, the Appellate Division held that a Deputy Attorney General could advise the Board while another Deputy Attorney General prosecuted before the Board.[96] Thus, both these cases involved agency heads and attorneys engaging in *ex parte* discussions on cases pending before the agency, or in which the agency would ultimately issue a decision, whereas the Board was not the ultimate decision-maker in the federal litigation initiated by VNJ, it was the District Court of New Jersey. Therefore, any discussions between representatives of the Board and VNJ in the context of settling the federal civil action did not invoke the *ex parte* rules.

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93 AT&T's January 13, 2004 Reply on Motion for Reconsideration at 3, footnote 2.

94 Opinion No. 583, 107 N.J. at 232.

95 Id. at 238-239.

96 Fiorillo, 242 N.J.Super. at 676.

Accordingly, based on a thorough review of the arguments articulated by AT&T and MCI, and for the reasons described hereinabove, we **HEREBY DENY** AT&T's Motion for Reconsideration and MCI's Motion for a Stay in their entirety.

DATED: **1/26/04**

BOARD OF PUBLIC UTILITIES
BY:

SIGNED

JEANNE M. FOX
PRESIDENT

SIGNED

FREDERICK F. BUTLER
COMMISSIONER

SIGNED

CAROL J. MURPHY
COMMISSIONER

SIGNED

CONNIE O. HUGHES
COMMISSIONER

SIGNED

JACK ALTER
COMMISSIONER

ATTEST:

SIGNED

KRISTI IZZO
SECRETARY